An FTC Guide to
Mergers

Entry and Efficiencies

ENTRY

IF A MERGER CREATES opportunities for the merged firm to raise price, other firms may be enticed to enter the market after the merger. This entry—if it is timely, likely and sufficient—may counteract the harmful effects of the merger and make enforcement action unnecessary. Under certain conditions, even the possibility of new firms entering the market will keep prices in check.

On the other hand, many factors can impede entry: licensing restrictions, zoning regulations, patent rights, inadequate supply sources, and cost of capital, among others. Entry may also take a long time, and consumers would be paying higher prices all that time. And, finally, the new firm may fail to attract customers away from existing firms, particularly in markets where existing firms have a proven track record. Assessing entry conditions calls for intensive fact-finding and is unique to each industry.

EXAMPLE: The FTC challenged a merger between two leading U.S. makers of field-erected industrial and water storage tanks. The Commission found that although new firms had attempted to compete for customers, they lacked the reputation and experience that most customers demand and were not capable of replacing the competition lost due to the merger. The Commission ordered the company to create two separate, stand-alone divisions that would restore competition to the market.

EFFICIENCIES

MANY MERGERS PRODUCE SAVINGS by allowing the merged firms to reduce costs, eliminate duplicate functions, or achieve scale economies. Firms will often pass merger-specific benefits on to consumers in the form of lower prices, better products, or more choices. The agencies are unlikely to challenge mergers when the efficiencies of the merger prevent any potential harm that might otherwise arise from the proposed merger. Theoretical cost savings would not be enough, however; they must be demonstrated. And the efficiencies must involve a genuine increase in productivity. It is not enough for cost savings to result merely from a reduction in output, or from the assertion of newfound market power against suppliers. The price reductions should result from real efficiencies in the merger and not from reducing output or service.

EXAMPLE: The FTC reviewed a proposed merger between two pharmaceutical companies that sold competing drugs used with solid organ transplants to reduce the patient's risk of rejection. The Commission found that the merger would reduce competition in the market for these life-saving drugs, and tailored a remedy to preserve competition in that market. The companies then merged to realize potential benefits in the related field of oncology treatment, where use of certain diagnostic tests could lead to more patients using these important drugs.

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